

MEDC Capital Services Programs

House Banking & Financial Services Committee

Representative Martin Knollenberg, Chair

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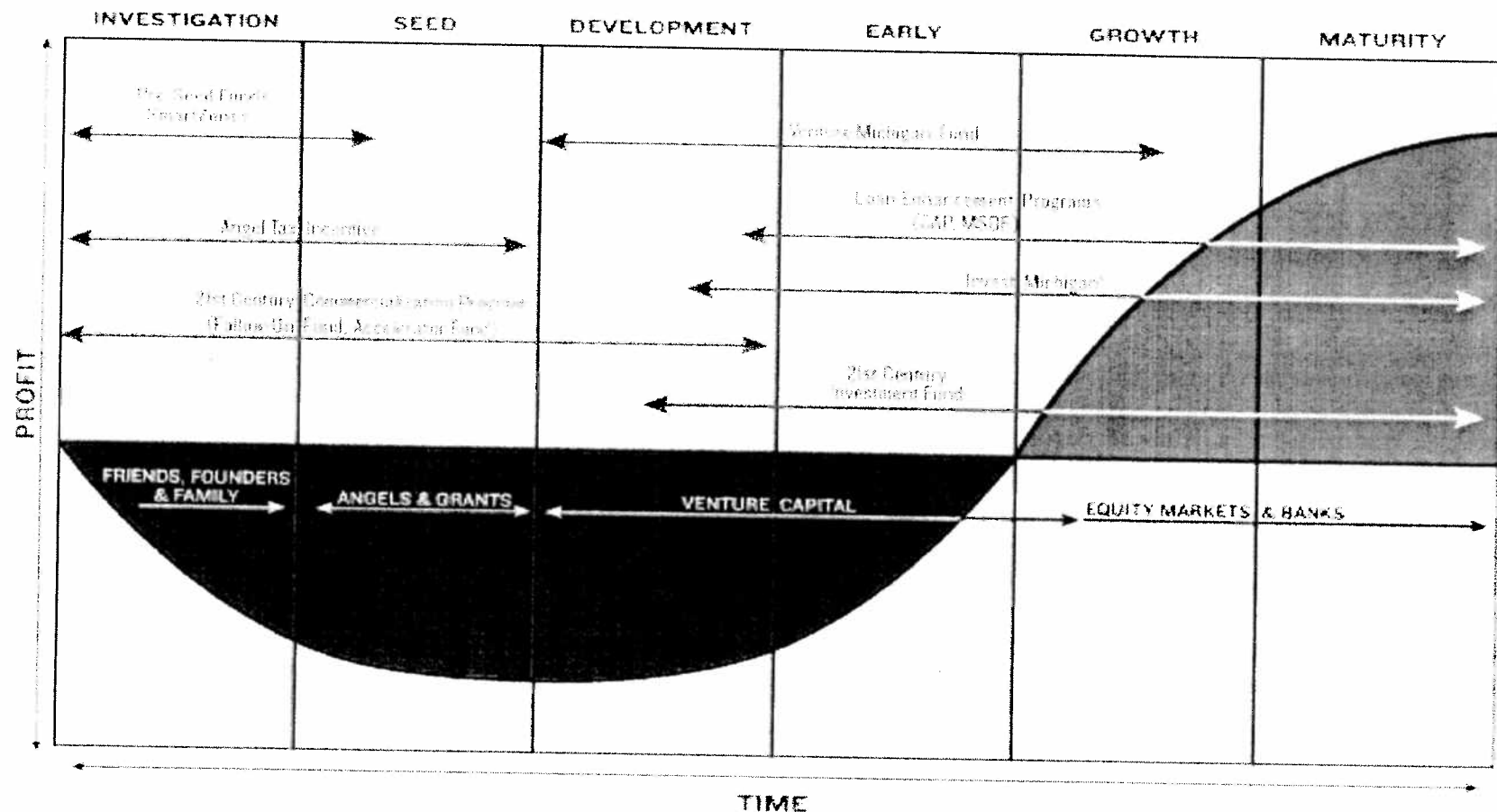
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The Capital Continuum



Capital Access Program

- Loan enhancement program:
 - Reserve pool concept allows lenders to draw funds in case of default
- Provides small businesses with access to capital for which they might otherwise be disqualified
- Administered by local financial institutions across Michigan with oversight from the MEDC

General Guidelines:

- Small business – less than 250 employees or \$6,000,000 in gross annual sales
- Must be legally authorized to conduct business in Michigan
- For Profit – Industrial, Commercial or Agricultural endeavors
- For business purposes only
- Cannot refinance current debt
- Not for residential housing or passive real estate

Creation of the Reserve Fund

- Banks' individual reserve funds consist of:
 - Borrower's fee: 1.5 to 3.5% of each loan
 - Lender's match: 1.5 to 3.5% of each loan
 - MEDC match: 3 to 7% of each loan
- Total of 6 to 14% of each loan reserved in bank's name in case of default
- Loan amounts have no minimum and a maximum of \$5 million

Example of Reserve Creation

- \$100,000 loan with 1.5% CAP fee
 - Borrower pays $\$100,000(0.015) = \$1,500$
 - Lender matches: \$1,500
 - MEDC matches total: $\$1,500(2) = \$3,000$
- Total in reserve:
 $\$1,500(2) + \$3,000 = \mathbf{\$6,000}$

Program Metrics to Date (since 2006)

- Loans Made = 1410
- Total Amount of Loans = \$97 million
- Total Public Investment = \$3.3 million
- Total Leverage Ratio = 29 : 1
- Total Jobs Created/Retained = 13,157

Michigan Supplier Diversification Fund

Purpose

- MSDF was designed to assist and stimulate private lending markets in financing diversification projects of viable businesses

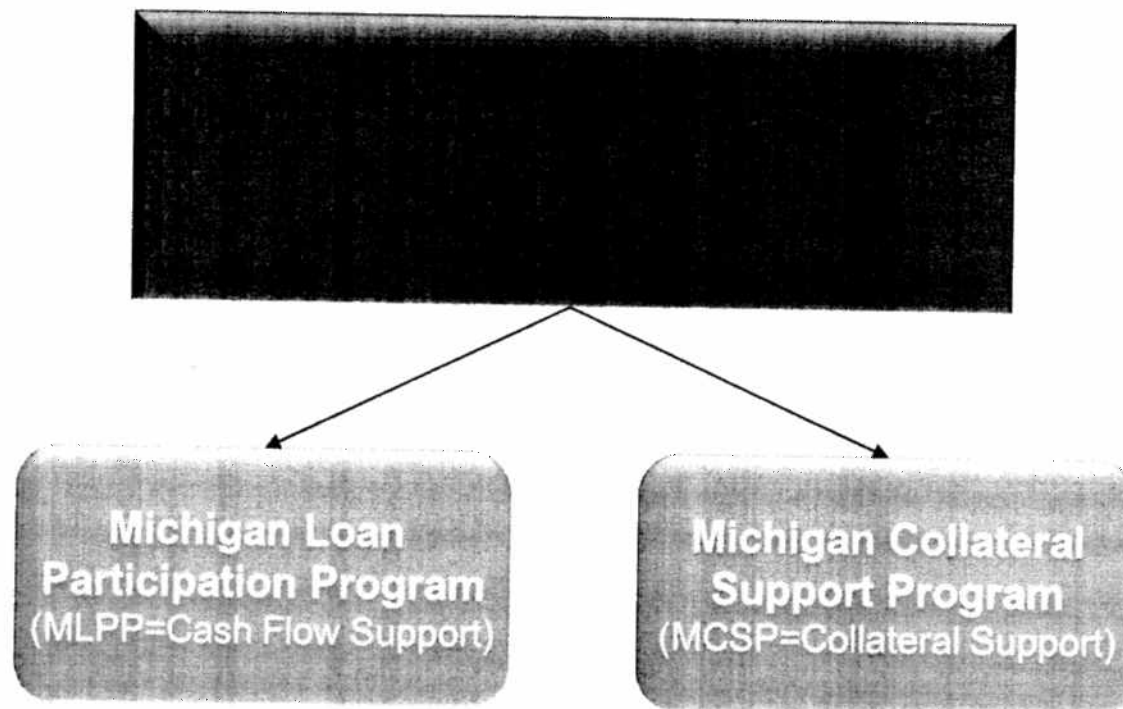
Design

- Addresses three impediments to lending programmatically:
 - **Cash Flow Shortage**: As defined by lender analyses, companies debt service coverage ratios too speculative
 - **Collateral Shortfall**: Collateral values declining

Key Elements

- Private lenders lead the deals
- Relies on bank underwriting and market discipline
- Non-Bureaucratic: Minimal paperwork and rapid turn around
- Programs were designed in consultation with private lending institutions to address the impediments to lending and corresponding solutions proposed by those institutions

MSDF Program Structure



- Under the new federal allocation, MSDF will be renamed the “Michigan Business Growth Fund” (MBGF), and continue to operate both MCSP & MLPP

Michigan Loan Participation Program

MLPP Program Description

- MEDC can purchase a portion of a credit facility (up to 49.9%) from a lender on new diversification projects that exhibit short-term cash flow deficiency according to the lender.
- MEDC can offer preferred terms on its portion of the credit facility (no interest and/or principal) for up to 36 months, thereby freeing up cash flow to cover debt service on the lender's portion.

Advantages to Lender

- Helps to limit project exposure during economic uncertainty.
- Ensures debt service coverage on lender's portion.
- Grace period allows higher risk deals to prove out, providing opportunity for lenders to limit risk during the early stages of a project while gaining access to potentially high reward deals.

Michigan Collateral Support Program

MCSP Program Description

- MEDC can supply cash collateral accounts to lending institutions to enhance the collateral coverage of borrowers attempting to diversify into new growth verticals.
- These accounts will cover all or a portion of a calculated collateral shortfall as described by the lending institution (up to 49.9% of credit facility).
- In the event of full default, the lender will have rights to the account less a liquidation fee.

Advantages to Lender

- Guaranteed collateral on up to 49.9% of credit facility in the event of full default.
- Increases deposits of lending institution during loan term.

Program Performance Metrics (as of 12/15/10)

- Loans Closed = 21
- Pending Commitments = 27
- **Loans Committed and Closed**
 - Program Dollars \$27,015,082
 - Direct Loans Induced \$66,648,379
 - Indirect Loans Induced \$97,069,506
 - Total \$190,732,967**
- Total Leverage Ratio = 6 to 1 private dollars to public dollars
- Total Fee Income = \$823,669 (to date, including annual fees)
- Nearly 2000 Jobs created or retained since program inception

Small Business Investment Tax Credit

- Signed into Michigan law in December, 2010
- Provides qualified investors an income-tax credit equal to 25% of an investment in qualified seed or early-stage Michigan business
- The Michigan Strategic Fund has oversight of the program, with administrative support from the MEDC
- Designed to increase early stage investments and investors in Michigan
- One of the most competitive programs of its kind in the country

SBITC Criteria & Provisions

- Taxpayers can claim a **25% credit** of a “qualified investment” in a “qualified business”
 - **Qualified Investment: Investment \geq \$20,000** certified by MSF made alongside or through a seed venture capital or angel group that is registered with and approved by the MSF; investment is not in business that employs or is owned by any member of investor’s family or with which investor or any member of investor’s family has preexisting fiduciary relationship; investment must remain in Qualified Business for minimum of 3 years unless a legitimate exit opportunity occurs.
 - **Qualified Business: Business certified by MSF Board** in compliance at the time of investment with the following:
 - **“Seed or early stage business”^a** (as defined by Michigan Early Stage Venture Investment Act)
 - **Headquartered/domiciled in Michigan** with majority of employees working in state
 - **Pre-investment valuation < \$10M**
 - **< 100 FTEs**
 - **< 5 years in existence**, or <10 years in existence if business activity originated from Michigan-based university or 501 (c)(3) organization
 - **Must be an innovative small business** with potential for high growth
 - **Is not operating:** a construction, transportation, hotel, motel, restaurant, or real estate business

Qualified Investors

- Must invest through or alongside a MSF-registered venture capital or angel group
- Must be an individual taxpayer or an incorporated entity subject to Michigan income tax laws as stated in Income Tax Act, PA 281 of 1967
- Must not be related to the owner(s) or employee(s) of the Qualified Business
- Must not have pre-existing fiduciary relationship with the Qualified Business
- For complete eligibility criteria visit: <http://www.michiganadvantage.org/Access-to-Capital/Default.aspx> (application forms and program fact sheet available here)

Other SBITC Considerations

- Taxpayers cannot claim a **credit >\$250,000 in a single qualified business** or >\$250,000 in aggregate qualified investments in qualified businesses in a single calendar year.
- Certification for tax credit must be requested by taxpayer within **60 days** of making investment.
- Tax credits exceeding a taxpayer's liability can be carried forward for up to **5 years**.
- Tax credit applied in equal installments over **2 years** commencing with tax year in which certificate issued.
- Maximum tax credits awarded per calendar year not to exceed **\$9M** (\$4M hard ceiling for investments through VCs + \$5M soft ceiling for investments through angel entity)

SBITC Expected Outcomes

- Minimum Annual Investment Induced = \$36 million
- Minimum Number of Early Stage Investments Annually = 36
- The State will have a clearer understanding of the investment landscape in Michigan for strategic purposes
- New accredited investors are expected to enter the fold, increasing the long term capital markets in MI
- A more stable and sustainable early stage investment ecosystem will result in the long term for early stage businesses



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